

**Letter of Findings: 01-20210026R
Individual Adjusted Gross Income Tax
For the Year 2019**

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HOLDING

Out-of-State Individuals were unable to establish that they were entitled to offset their Indiana gambling winnings against their gambling losses as ordinary and necessary business expenses; the Department determined that Individuals were recreational and not professional gamblers under the federal "hobby income" regulation.

ISSUE

I. Indiana Adjusted Gross Income Tax - Professional Gambler Status.

Authority: IC § 6-8.1-5-1; IC § 6-3-1-3.5; [45 IAC 3.1-1-1](#); I.R.C. § 62; I.R.C. § 165; Treas. § Reg. 1.183-2; *Dept. of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579 (Ind. 2014); *Popovich v. Indiana Dept. of State Revenue*, 52 N.E.3d 73 (Ind. Tax Ct. 2016); *Indiana Dep't of State Revenue v. Rent-A-Center East, Inc.*, 963 N.E.2d 463 (Ind. 2012); *Lafayette Square Amoco, Inc. v. Indiana Dep't of Revenue*, 867 N.E.2d 289 (Ind. Tax Ct. 2007); *Ferguson v. C.I.R.*, T.C. Summ. Op. 2007-30, 2007 WL 610059 (2007); *Busch v. Commissioner of Revenue*, 713 N.W.2d 337 (Minn. 2006); *Golanty v. Commissioner*, 72 T.C. 411 (1979).

STATEMENT OF FACTS

Taxpayers are out-of-state individuals who filed a joint 2019 IT-40 PNR ("Part-Year or Full-Year Nonresident") Indiana income tax return. On that return, Taxpayers reported Indiana source income primarily attributable to Indiana casino winnings.

The Indiana Department of Revenue ("Department") reviewed the 2019 return. The Department determined that Taxpayers were not "professional gamblers" and thereby not entitled to claim a deduction based on the total amount of 2019 "losses" incurred at the Indiana casino.

The Department's conclusion resulted in an assessment of \$500 in Indiana income tax on the total winnings and the denial of an approximately \$200 refund request originally claimed on the Indiana return.

Taxpayers disagreed with the adjustment and submitted a protest to that effect. An administrative hearing was conducted by telephone during which Taxpayers' representative explained the basis for the protest. This Letter of Findings results.

I. Indiana Adjusted Gross Income Tax - Professional Gambler Status.

DISCUSSION

The issue is whether husband and wife Taxpayers have provided sufficient information to establish that they are "professional" gamblers entitled to offset their total Indiana gaming losses against their total Indiana gaming winnings.

A. Reporting Indiana Gambling Winnings and Losses.

IC § 6-3-1-3.5 states as follows, "When used in [IC 6-3](#), the term 'adjusted gross income' shall mean the following: (a) In the case of all individuals 'adjusted gross income' (as defined in Section 62 of the Internal Revenue Code) Thereafter, the statute specifies addbacks and deductions, peculiar to Indiana, which modify the federal adjusted gross income amount. The Department's regulation concisely restates the formulary principal. [45 IAC 3.1-1-1](#) defines individual adjusted gross income as follows:

For individuals, "Adjusted Gross Income" is Adjusted Gross Income as defined in Internal Revenue Code § 62 modified as follows:

- (1) Begin with gross income as defined in section 61 of the Internal Revenue Code.
- (2) Subtract any deductions allowed by section 62 of the Internal Revenue Code.
- (3) Make all modifications required by [IC 6-3-1-3.5\(a\)](#).

Both the statute, IC § 6-3-1-3.5, and the accompanying regulation, [45 IAC 3.1-1-1](#), require that an Indiana taxpayer employ the Federal adjusted gross income calculation, as determined under I.R.C. § 62, as the starting point for determining the taxpayer's Indiana adjusted gross income.

I.R.C. § 62 states that, "For purposes of this subtitle, the term 'adjusted gross income' means, in the case of an individual, gross income minus the following deductions" The deductions specified under I.R.C. § 62 contain no provision permitting an individual to deduct gambling losses from his or her gross income. However, the federal law does permit the deduction of gambling losses to the extent of a taxpayer's gains from similar transactions. I.R.C. § 165(d).

[Professional Gambling] expense deductions . . . are above-the-line deductions made pursuant to the provisions of the Internal Revenue Code and the related U.S. Treasury Regulations in determining federal adjusted gross income. *Popovich v. Indiana Dept. of State Revenue*, 52 N.E.3d 73, 79 (Ind. Tax Ct. 2016).

B. "Professional" Gamblers and Recreational Gamblers.

Tax reporting by a professional gambler is different from that of a recreational gambler. A recreational gambler can report losses only to the extent of gains from gambling activity. The recreational gambler reports winnings as part of adjusted gross income and may report losses only if deductions are itemized. The professional gambler is not required to report losses as an itemized deduction. Instead, losses and gains are reported on Schedule C. The net gain or loss is then reported on Form 1040 prior to arriving at adjusted gross income as an above-the-line deduction. This typically causes the professional gambler's adjusted gross income to be lower than that of the recreational gambler because the professional gambler is able to deduct "necessary and ordinary" business expenses from gambling gains.

Determining whether a taxpayer is a professional gambler - is engaged in a "trade or business" - or whether the taxpayer is simply a recreational gambler is determined under I.R.C. § 183 which are the "hobby loss" rules.

Treas. Reg. § 1.183-2 provides a "non-exhaustive list of factors to be *weighed* when determining whether a taxpayer was engaged in gambling with the objective of making a profit." *Popovich*, 52 N.E.3d at 79 (*emphasis in original*). Treas. Reg. § 1.183-2(b). The regulation's factors include:

- The manner in which the taxpayer carries on the activity including whether the taxpayer carries on the activity in a "businesslike manner and maintains complete and accurate books;
- The expertise of the taxpayer including whether the taxpayer prepares for gambling "by extensive study";
- The time and effort spent by the taxpayer in carrying on the activity;
- The expectation that the money spent gambling may result in profit;
- The success of the taxpayer in carrying on the gambling activity;
- The taxpayer's history of gambling winnings and losses;
- The amount of any profits from gambling;
- The financial status of the taxpayer. Does the taxpayer have "income or capital from sources other than the [gambling] activity";
- The relative elements of "personal pleasure or recreation" attributable to the gambling activity. See also *Popovich*, 52 N.E.3d at 79.

Taxpayers argue that they are entitled to claim professional gambling status, but the Department disagrees and concludes that - based "on the best information available" - they are engaged in gambling as a recreational "hobby."

C. Taxpayers' Burden of Establishing that the Department's Decision was Wrong.

As with any assessment, it is Taxpayers' responsibility to establish that this particular \$500 tax assessment is incorrect. As stated in IC § 6-8.1-5-1(c), "The notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made." *Indiana Dep't of State Revenue v. Rent-A-Center East, Inc.*, 963 N.E.2d 463, 466 (Ind. 2012); *Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue*, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

Furthermore, the Department bears in mind its statutory responsibility under IC § 6-8.1-5-1(b) which states that if it "believes that a person has not reported the proper amount of tax due, the department *shall* make a proposed assessment of the unpaid tax on the basis of the best information available to the Department." (*Emphasis added*).

In making their case, each taxpayer is required to provide documentation explaining and supporting his or her challenge that the Department's position is wrong. Further, "[W]hen [courts] examine a statute that an agency is 'charged with enforcing . . . [courts] defer to the agency's reasonable interpretation of [the] statute even over an equally reasonable interpretation by another party.'" *Dept. of State Revenue v. Caterpillar, Inc.*, 15 N.E.3d 579, 583 (Ind. 2014). Thus, informed and reasonable interpretations of Indiana tax law contained within this decision, as well as the preceding audit, are entitled to deference.

D. Taxpayers' Arguments.

Taxpayers explain that they garnered a \$15,000 profit by gambling at the Indiana casino. Taxpayers maintain that the mere fact that they made a gambling *profit* would tend to show that they were professional gamblers. In addition, Taxpayers have provided their W-2G ("Certain Gambling Winnings") detailing their winnings at an Indiana casino. Taxpayers have not provided additional, verifiable, and contemporaneous documentation to support the proposition that they are professional gamblers.

E. Analysis and Conclusion.

The Department is unable to agree that Taxpayers have met their statutory burden of establishing that they engaged in casino gambling for the purpose of making a profit. Taxpayers have not provided a written business plan or developed business strategies which could be used to support their assertion that they could earn a living betting their money at an Indiana casino. Taxpayers have not provided evidence that they engaged in "extensive study" to improve their odds by playing casino games and thereby assure them of a viable income.

Further, Taxpayers have provided no evidence that they maintained their own gambling records but instead simply relied on the casino's statements to track their gains/losses and gambling activities. Presumably, someone in the business of professional gambling would maintain original documentation such as airline or other travel documentation, a gambling log or diary, hotel charges, cash credit card advances, bank withdrawals, casino statements, programs; it is not unreasonable to assume that a taxpayer engaged in a professional activity intended to provide that person with a living would likely keep their own contemporaneous business records.

Taxpayers failed to assert anything other than that they *intended* to make a profit. However, any such a profit intention must be genuine, actual, if not reasonable. *Busch v. Commissioner of Revenue*, 713 N.W.2d 337 (Minn. 2006). Whether a taxpayer has an honest and objective intent is redetermined on a year-to-year basis. *Golanty v. Commissioner*, 72 T.C. 411, 425 (1979).

The Department remains unconvinced as to whether it is possible to have an actual and honest intention to make a profit playing casino games or that one can realistically rely on their \$15,000 in winnings to maintain their livelihood. In determining whether a petitioner established an honest and actual intention to make a profit playing casino games, the United State Tax Court explained in *Ferguson v. C.I.R.*, T.C. Summ. Op. 2007-30, 2007 WL 610059 (Feb. 28, 2007).

We are additionally unconvinced that petitioner's gambling activity meets the standard for being a trade or

business because we are not persuaded that an individual who gambles against a machine that is programmed by a casino can have, as his or her primary purpose, income or profit. After all, such a machine is on the floor to make money for the casino and is not there to provide income or profit for the casino's patrons. For most individuals, gambling against a machine that is programmed to make money for the casino constitutes what the Supreme Court in *Commissioner v. Groetzinger*, 480 U.S. 23 (1987), characterized as a sporadic activity, hobby, or amusement diversion. For other individuals, gambling against such a machine may become a habit or an addiction. In neither scenario is it a trade or business with the participant's primary purpose being income or profit.

Taxpayers have not met their burden under IC § 6-8.1-5-1(c) of establishing that the Department's assessment was wrong. The Department is in no position to question anyone's intentions or how they spend their money, but there is little evidence that Taxpayers played casino games and maintained gaming records in a "businesslike manner," that they prepared to gamble by undertaking "extensive study," or that they had an actual and realistic expectation that the Indiana casino could reasonably be relied upon to provide their livelihood.

After weighing the relevant factors set out in the federal regulation, the Department must decline to sustain Taxpayers protest.

FINDING

Taxpayers' protest is respectfully denied.

March 12, 2021

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